First Female Prime Minister and Takaichi Trade

Nikkei Approaches ¥50,000: Key Points to Consider Going Forward

October 22, 2025

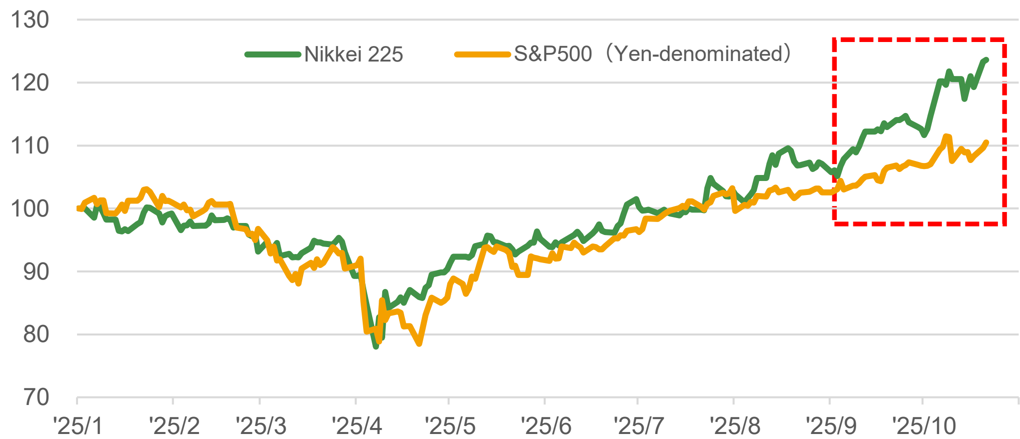
Japanese Stocks in a Medium-Term Uptrend: Political Progress Adds Extra Fuel

LDP President Sanae Takaichi was elected as the 104th Prime Minister of Japan, making her the country's first female prime minister. The Nikkei 225, which had fallen back to a level below 47,000 Yen the previous week due to political uncertainty, rebounded vigorously to new highs this week, and on the 21st, when the prime ministerial nomination election was held, the Nikkei 225 briefly rose to just below 50,000 Yen. Since former Prime Minister Shigeru Ishiba announced his resignation on September 7, the phase of domestic political developments that had been causing both joy and sorrow seems to have come to an end for the time being.

Regardless of political developments, it is important to note that the Japanese stock, share market is in the midst of a medium-term rally, and the domestic inflation and corporate governance reforms that have been boosting Japanese stocks since 2023 will continue to support stock prices through ROE expansion and other factors. AI-related markets are expected to grow strongly, and the Fed has begun its interest rate cut cycle. On top of that, positive political developments will provide additional tailwinds. Foreign investors have been positive about Japanese equities because of their appreciation of the macro and micro changes underway in Japan, but in addition to policy expectations, the arrival of the first female prime minister in the country's constitutional history will give foreign investors a renewed and stronger appreciation of the changes in Japan.

With the political-related catalysts having run their course, the near-term outlook is to digest the expectation-driven rally, while keeping an eye on policy developments and corporate earnings in the mid-term financial results, settlement of accounts, etc. Many investors are likely to be unable to buy stocks because of the rapid pace of their rise, and even when stock prices adjust, push-back buying will provide support, limiting the extent of the decline.

Since Summer, Nikkei 225 Has Outperformed the Yen-Denominated S&P 500



※ Indexed at the beginning of 2025 as 100, latest value as of October 21.

Source: Bloomberg; Compiled by Daiwa Asset Management

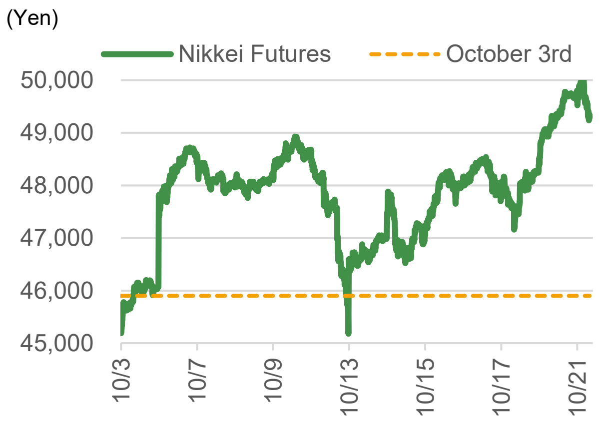
Takaichi Trade Delivers Different Outcomes Across Asset Classes

Immediately after the LDP presidential election, markets saw a rapid move dubbed the “Takaichi Trade,” characterized by a surge in equities, Yen depreciation, and a steepening of the yield curve (short-term rates falling and long-term rates rising). However, subsequent developments have varied across asset classes.

The most pronounced positive reaction has been in equities. Although there was a temporary pullback following the departure of KOMEITO from the coalition, stock prices resumed their climb as talks with Japan Innovation Party (JIP) progressed and have moved even higher this week. In contrast, the bond market has moved in the opposite direction of expectations: yields on super-long bonds and yield spreads have fallen back below pre-election levels. This appears to reflect the growing influence of Vice President Aso, a fiscal hawk, the emphasis on fiscal discipline by JIP as a coalition partner and fading overly cautious views on BOJ rate hikes.

The USD/JPY exchange rate remains weaker than before the election, but the momentum lasted only until midweek of the first week. In addition to domestic rate movements, escalating US-China trade tensions and US administration warnings against excessive Yen weakness have played a role. From an equity market perspective, the restrained tone in bonds and FX is seen as a positive factor.

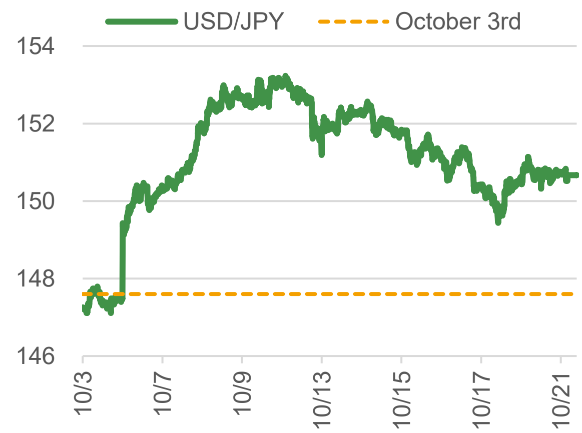
Equity Market Reacted Most Positively to Prime Minister Takaichi



※ October 3 at 3:30 p.m.; latest value as of 3:30 p.m. on October 21.

Source: Bloomberg; Compiled by Daiwa Asset Management

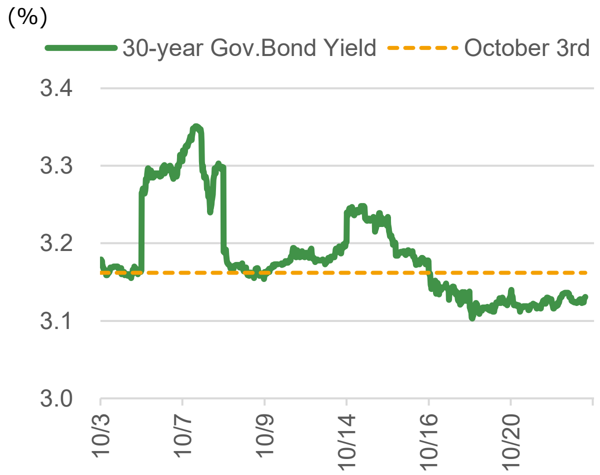
USD/JPY Rate Has Retraced About Half from Its Peak



※ October 3 at 3:30 p.m.; latest value as of 3:30 p.m. on October 21.

Source: Bloomberg; Compiled by Daiwa Asset Management

Yields on Ultra-Long Bonds Below Pre-Election Levels



※ October 3 at 3:30 p.m.; latest value as of 3:30 p.m. on October 21.

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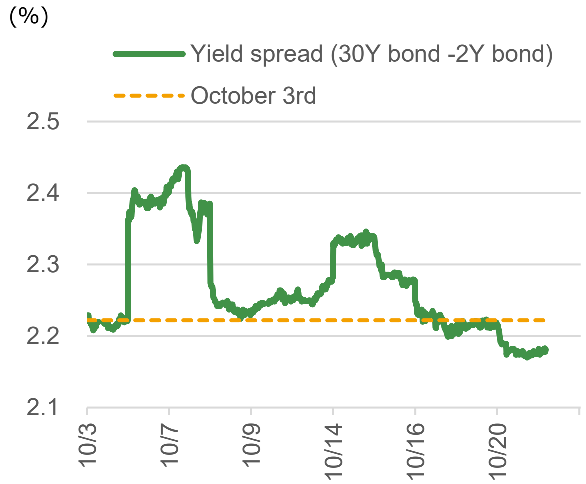
Yield spreads are also at the same level



※ October 3 at 3:30 p.m.; latest value as of 3:30 p.m. on October 21.

Source: Bloomberg; Compiled by Daiwa Asset Management

Upside and Downside Risks for Japanese Equities

Although the LDP led by President Takaichi dissolved its coalition with KOMEITO, it reached an agreement with Japan Innovation Party (JIP) , leaving the ruling bloc just two seats short of a majority in the Lower House. This development is seen as increasing the likelihood of various policy initiatives being realized. In our October 10 Market Letter, we stated: “If political and policy progress continues steadily and confidence in accelerated earnings growth for FY2026 strengthens, a Nikkei level above ¥50,000 becomes increasingly realistic.” That scenario now appears more likely.

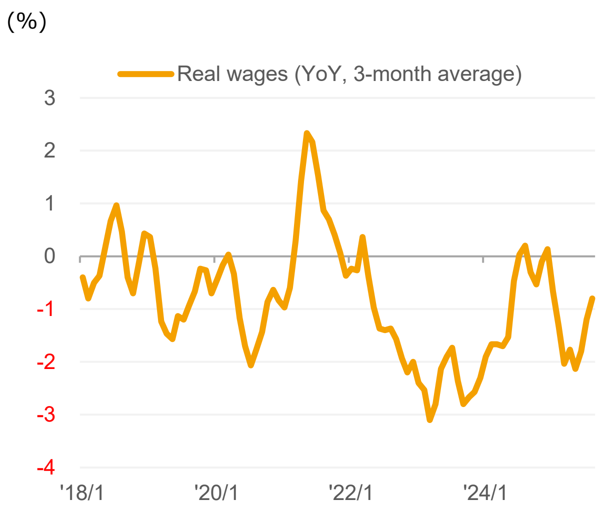
That said, for the Nikkei to not only touch ¥50,000 but sustain that level, several conditions still need to be met. The recent rally has been somewhat expectation-driven, so if politics and earnings fail to meet those expectations, valuations could compress and trigger a market correction. The upcoming interim earnings season, which kicks off in earnest next week, will be critical. The equity market is already pricing in next fiscal year’s earnings, so if expectations falter, maintaining current PER levels will be difficult. Politically, the coalition agreement is only the starting point. We need to confirm whether policies will be implemented and how they will impact the economy and corporate earnings.

The first priority is measures to counter rising prices. Economic support for households is often saved rather than spent, limiting its impact, but given the ongoing domestic inflation and shifting norms among consumers and businesses, fiscal policies aimed at household support are likely to be effective. Despite continued strong wage growth, soaring prices for essentials such as food have kept real wages on a downward trend, and consumption remains sluggish. Current inflation is largely cost-driven, hurting household finances, but policies that boost disposable income could spur behavioral changes among consumers, leading to price hikes and revenue growth for companies, and ultimately fueling further wage increases—a virtuous cycle.

Over the medium term, growth strategies to lift Japan’s economy will be key. Abenomics was initially welcomed by overseas investors, but interest in Japanese equities waned as progress on structural reforms—the “third arrow”—proved insufficient. Prime Minister Takaichi appears to favor a growth model driven by investment through fiscal measures. We will be watching developments closely.

(Written by Kazunori Tatebe, Research Department)

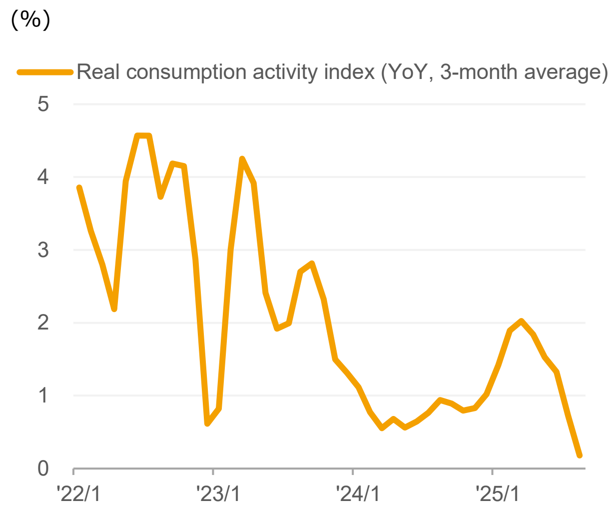
Real Wages Continue to Decline…



※ Latest value as of August 2025

Source: Ministry of Health, Labor and Welfare; Complied by Daiwa Asset Management

Consumption Lacks Strength…



※ Latest value as of August 2025

Source: Bank of Japan; Complied by Daiwa Asset Management

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